

A STUDY OF THE MARKETING ACTIVITIES OF
PRIVATE BANKING IN HONG KONG

by

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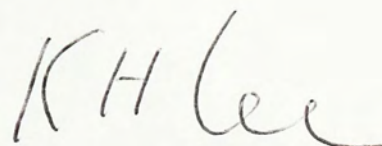
RESEARCH REPORT

Presented to
The Graduate School

In Partial Fulfilment
of the Requirement for the Degree of
MASTER OF BUSINESS ADMINISTRATION

TWO-YEAR MBA PROGRAMME
THE CHINESE UNIVERSITY OF HONG KONG

May 1988



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ABSTRACT

A Private Banking Institution (PBI) is an institution giving financial advice or services to High Net Worth Individuals (HNWIs). A HNWI is someone whose disposable asset is great enough to deserve personalized services from a PBI.

Private banking industry has experienced a fast growth recently. Many major banks in Hong Kong started up their private banking operations to capture the growing market. However, a successful PBI should have high proficiency in planning and executing its marketing activities.

The scope of this research is to study those marketing activities in Hong Kong. During the study, a lot of literatures on issues of service marketing are reviewed and summarized. At the same time, field studies consisting mainly of in-depth discussions with the management of private banks were conducted.

The literatures are used as references for building a conceptual framework of the marketing activities of private banking. Based on such a framework, the present situations are evaluated and recommendations on marketing strategies and approaches will then be suggested.

Though this study is preliminary in nature, it is still considered to be a useful interim step towards improved private banking in Hong Kong.

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ACKNOWLEDGMENT

I am particularly indebted to my research advisor, Dr. Kam-Hon Lee, Reader in the Department of Marketing and International Business and Director of the MBA Programmes, for his guidance and encouragement -- without which this research would not have completed.

During the course of this study, stimulating conversations with professional bankers from different banks have enhanced much of my understanding about private banking in Hong Kong. Special thanks go to all these experts whom I have interviewed. Their valuable information and kindly help are much appreciated.

Despite all the help and suggestions offered to me, it is possible that errors and omissions occur in this research report. This certainly remains my responsibility.

CHAPTER I

INTRODUCTION

"Another vital issue concerns rapid changes in delivery bank services. There are two kind of service delivery, human and electronic, and the banks are moving in two directions at the same time, first towards far greater personal service in which customers' personal bankers do all banking services for them..... We need to find a way to afford all that expensive personal service."¹

1.1 What is Private Banking?

With the advance of technology, many banks change their ways of service delivery by introducing automatic teller machines for individual customers and electronic banking for corporate clients.

While the increasing operational cost forces banks to standardize and package their products to numerous customers, the specific needs of different customers lead banks to personalize their service to satisfy them.

However the cost of service should be somehow paid by the customers. Thus only those customers, better described as clients, of high net worth can afford such high costs of personalized services and high prices of tailor-made products. The men in the streets can only be served by ATMs and offered standardized products.

To the very end of personalized services to individuals is called PRIVATE BANKING.² Those High Net Worth Individuals (HNWIs) will be served by a Personal

Account Executive (or a Accounts Manager). Through the Account Executive, the resources of the banks will be made available to HNWIs. Such a situation, as private bankers always denoted, is called one-stop financial shopping.

Here is how the Hongkong Bank describes its private banking services,

The aim of the bank on behalf of its Private Banking clients is to preserve and enhance their private wealth. Private Banking Services are provided with a high level of individual attention emphasizing confidentiality and with a wide range of banking and investment alternatives around the world. (Source : company's pamphlet)

1.2 Definition of Marketing

The new official American Marketing Association (AMA) definition of marketing is (Brown 1985),

Marketing is the process of planning and executing the conception, pricing, promotion, and distribution of ideas, goods, and services to create exchange that satisfy individual and organizational objectives ("AMA Board" 1985)

This definition does underscore the strategic nature of marketing. Marketing can direct organizational resources and effort to attain its goals and missions.

Marketing requires both planning and executing. In the planning stage, an organization needs to determine the needs and wants of target markets so as to deliver the desired satisfactions more effectively and efficiently than competitors. During the execution, the organization needs to develop a suitable marketing mix and manage its marketing effort.

For a private banker, his/her products are services and ideas. By the very nature of his/her products being services and ideas, there are some well-documented

characteristics (Zeithaml et al 1985a) that poses a set of problems for service marketers to solve. The characteristics include intangibility, inseparability, heterogeneity and perishability. The set of problems then follows will be discussed in Chapter IV.

1.3 Purposes and Scopes of the Study

After a brief introduction of private banking and marketing, the aims of this study can be described as,

(1) to offer some conceptual frameworks summarizing the unique characteristics of private banking as a service, the problems stemming from these characteristics and the marketing tactics and strategies suggested as appropriate to overcome the problems,

(2) to report the findings of field studies consisted mainly of in-depth discussions with managements of private banks in Hong Kong concerning the problems they face and the marketing strategies they use to overcome them,

(3) to compare findings of field studies with the conceptual frameworks previously established, and

(4) to offer recommendations, by exploiting alternatives of generic marketing strategies and feasible marketing approaches, for further development of the private banking industry in Hong Kong.

It is hoped that some policy and strategy implications concerning private banking in Hong Kong can be derived from the findings of this research.

As a strategic business unit within the business

portfolio of an individual bank, a private banking division should be carefully evaluated and positioned to attain the bank's corporate missions and objectives. On the other hand, given well-defined business objectives, the private banking division needs to formulate a marketing plan and carry out a complete marketing management process to match itself to its best market opportunities.

It is anticipated that recommendations can be made in the area of products development policy, personnel policy, promotion policy and pricing policy. Through a better understanding by private banks of the needs of HNWIs, it is also hoped that exchanges then created can satisfy both HNWIs' and banks' own corporate objectives.

During the study, a lot of literatures on issues of service marketing are reviewed and summarized. They are then used as references for building the conceptual frameworks for the marketing activities of private banking. Based on such frameworks, the present situations are evaluated and recommendations on strategies for growth will also be suggested.

1.4 Limitations of the Study

Besides those marketing aspects that are included in this study, there are of course many more constraints and factors that determine the optimal strategy of the private banking operation of a particular bank.

Thus this study can only be considered as a preliminary investigation into some selected issues about

the marketing activities of private banking in Hong Kong. Furthermore, the recommendations suggested are based on the limited information available to the author. Different banks should integrate their own proprietary information into the frameworks discussed in the study before finalizing their own marketing plan.

Nevertheless, this study is still considered to be a useful interim step towards improved private banking in Hong Kong.

1.5 Plan of the Report

This report comprises of six chapters of different areas. After a brief introduction of purposes and scopes of the study in this chapter, the research methodology will be discussed in the next chapter. After explaining the general industry environment of private banking in Chapter III, it will establish a conceptual framework in Chapter IV, and report the results of field studies in Chapter V. Chapter VI is the ending chapter for the recommendations and comments.

¹A banker's comments on current marketing issues of banking industry. Source : Journal of Marketing, vol.45 (Winter 81) p.144.

²There is still a market segment for the individuals of worth lower than that of HNWI but still desire more personalized services to them than to ordinary customers. The bankers called this service as PERSONAL BANKING. Examples are Personal Financial Centres of First Pacific Bank, Standard Chartered Bank in the lower end, and Golden Circle Service of Chase Manhattan Bank on the upper end of the spectrum.

CHAPTER II

RESEARCH METHODOLOGY

2.1 Research Design

With an aim to offer the conceptual frameworks summarizing the unique characteristics of private banking as a service, the research design of the study consisted of three parts, (1) literature searches, (2) fields studies, and (3) a comparison of fields studies with propositions in literatures.

Literature searches focus mainly on marketing issues of service industry, while field studies focus on the observed behaviors of the different private banks in Hong Kong.

2.2 Literature Searches

The literature searches start from reading books on general marketing (Bagozzi 1985, Kotler 1986) and services marketing (Channon 1986, Kotler 1984). Those books have very good explanations of conceptions and practices in marketing. They also underscore important issues and provide strategies for solving marketing problems.

Then the searches concentrated on the reviews of periodicals, mainly those in Journal of Marketing and Harvard Business Review. Those articles cover topics of current marketing issues like competitors analysis, market

planning and personalization in service industry.

The ideas and concepts put forwards in the book and periodicals will be reviewed and summarized in Chapter IV.

2.3 Field Studies and Interviews

Most of the information included in this report are obtained by field studies and interviews. To begin with the study, a handful of pamphlets are collected in the exhibition "Money 87" held in October, 1988.

The pamphlets contain a lot of useful information on products offered by several private banks. There are also concepts and beliefs of private banks towards their own services.

Additional information about private banking are obtained by reading through columns in South China Morning Post and Asian Finance. Those columns usually contain private bankers' comments and explanations of their services and target markets. However, the information is by far completed and structured to give a clear image of private banking to readers.

Thus the core parts of field studies are personal interviews arranged with management of leading private banks. The purpose of the interviews is to obtain first hand information about marketing issues of private banking.

Prior to the formal interviews based on standardized questions, three exploratory interviews are carried out. They are banks which are reached by phone and kindly offer interviews with the author. The interviews are helpful

in providing a general feel about the nature and background of the industry. A set of questions is then set for coming interviews with other banks¹.

Twelve letters asking for an interview are sent, of which five have positive results. The twelve banks are selected by identifying the major players in private banking in Hong Kong and by including banks with different countries of origins.

The following chapter will discuss the environments and opportunities of private banking in Hong Kong.

¹The set of interview questions are :

From the point of view of your bank as a major (American) bank in Hong Kong,

- (1) How do private banking and/or a private banking institution be defined?
- (2) How does a potential client be qualified as HNWI?
- (3) What are the products that fit the needs of your clients?
- (4) What are the attributes of a successful account manager?
- (5) What are the major promotion efforts in Private Banking?
- (6) What is a reasonable fee as perceived by your clients?
- (7) What are the opportunities and threats existed in the world market for the private bankers in Hong Kong?
- (8) How do the recent economics and social changes affect the industry as a whole?

CHAPTER III

THE PRIVATE BANKING IN HONG KONG

In the Chapter I, the author has roughly described what is private banking. In this chapter, more space will be devoted to the description of the environments for private banking and the opportunities and threats for private bankers in Hong Kong.

3.1 Definition of Private Banking

A PRIVATE BANKING INSTITUTION (or a Private Bank) is defined as,

A PRIVATE BANKING INSTITUTION (PBI) is an institution giving financial advice or services to High Net Worth Individuals (HNWIs). A qualified PBI should at least be a separate department or a strategic business unit having its own resources and objectives within a financial institution.

The definition of a HIGH NET WORTH INDIVIDUAL is,

A HIGH NET WORTH INDIVIDUAL is someone whose disposable asset is great enough to deserve personalized services from a PBI.

And as a related term, PRIVATE BANKING is defined as,

PRIVATE BANKING is referred either to the services provided by a PBI or the industry of providing such services.

3.2 Private Banking Institutions (PBIs) in Hong Kong

A PBI in Hong Kong can be a department within a licensed bank. Examples are that within Hongkong Bank, Standard Chartered Bank, International Bank of Asia, Bank of America and many more. A PBI can be a brokerage or security house, like Yamaichi, Nikko and Merrill Lynch. A Deposit Taking Company, registered or licensed, can also be a PBI if it has a separate department to provide personalized services to its clients.

Chartered Bank's PBI, as a 'private bank within a bank' (company's pamphlet), is structured under individual banking group. Other examples are the Chase Manhattan Bank and Citibank.

However, a PBI within an international bank usually has easy access to the vast resources and expertise of the bank worldwide. It also has offices strategically located around the world. For example, Barclays International Private Banking section "has its own specially created offices in London, Switzerland, New York, Miami, Hong Kong, the Cayman Islands, and the Channel Islands." (company's pamphlet)

PBIs in Hong Kong usually serve not only clients in Hong Kong, but also those in other Asian countries, like Taiwan, Singapore, Korea, Thailand, Philippines and Indonesia. They may also set up sub-offices in those countries to better serve their client, but almost all the transactions are carried out in Hong Kong for its low operational cost and good communications.

Most PBIs in Hong Kong are newly set-up. For example, Standard Chartered Bank has started its PBI for only one year, while most others started theirs for three to four years. One of the exceptions is CitiBank Private Banking Office which has started since 1968 (Geraghty 1985).

However, private banking in Hong Kong started about 20 years ago, when secret accounts in Switzerland were used by Asian people. Since then, private banking in Asia shifted from just buying gold for their clients to offering a wide range of products, from retail to fiduciary, from investment services to trust-setting.

Different PBIs seem to have similar ideas on what is private banking. Miss Alice Tsang of Hongkong Bank puts it as "providing a private and professional service for a private individual so that his/her financial needs can be met."

Private Banking is virtually an international service depending on the worldwide networks of a PBI. Thus, some banks call themselves International Private Banking or Private Banking International.

3.3 How to be Qualified as Private Banks' Clients

In real practices, many of the private banks interviewed use a more quantified approach to define their clients. The most common one is, "HNWIs are those with liquid assets exceeding US\$ 1 millions."¹ A few may expect more from their clients. For instance, the client-pool of Bank of America is "that could hand over US\$ 5 million up

to the bank or banks of their choice." (McGlothern 1987).

Some American banks may not accept United States' citizens as clients for tax reasons. On the other hand, some European banks just focus on clients who decline to bank with a PBI from their country of origin.

3.4 Growth of Private Banking in Hong Kong

Here are factors that are found to be reasons for Hong Kong's success in becoming one of the most important international financial centres (Lee and Vertinsky 1988),

1. English is the working business language.
2. Access to political decision makers by local and foreign financial institutions.
3. A country that requires a minimum degree of financial disclosure.
4. Openness of the local business community to foreigners.
5. Availability of inexpensive support services.
6. Proximity to a large base of borrowers.
7. A city with well-developed post-secondary education systems.

Most of the above factors are also applied to be the reasons why Hong Kong becomes a private banking centre in Asia. Other factors include good geographical location and the strong economic growth of the Hong Kong together with other parts of Asia.

In Asia, people can easily accumulate funds because of the low taxation and the rapid growth of their economy. Some economists are so optimistic about Pacific basin that they call next century as the "Pacific Century".

The private banking industry in Hong Kong is growing as both the wealth of the people and their needs of personalized service increases. Many private bankers forecast a continued growth of private banking in Hong

Kong and Asia.

Many PBIs experienced a strong growth of their business for last few years. One banker quotes the author a compound growth rate of over 60 % for their business volume since its operation in Hong Kong opened three years ago.² Though he does not foresee a continued high growth rate of the business, he is very confident of a bright future of his business.

3.5 Opportunities and Threats of Private Banking in Hong Kong

In addition to a high growth rate of the market, there are other reasons making private banking a market opportunity for banks.

** Profits at investment banks have proved extremely volatile because the way to make money is to risk the bank's own capital by betting on which way prices will move. Between the first and second quarters of 1987, for instance, the profits of big New York investment banks dropped by 82 %. Private banking are making only investment management services, and the volatility of the market is at clients' risk rather than PBIs'.

** In recent years witnessed the contraction of commercial banking world-wide and their increased reserves for third-world debts. The performances of banks are seriously hurt. They started to find that incomes from spread between deposits and loans are diminishing and the risk factors are increasing. Their returns on assets are also very disappointing. Swapping from spread-earning to

fee-earning will greatly improve the situation. More banks are therefore willing to put more stakes on private banking.

** There are many social and economical changes that favour the growth of private banking. The high economic growth of Asian countries in the last decade accumulates a substantial amount of wealth around. One good example is Taiwan, where there are a continued surplus of funds and recent deregulations of financial markets. Together with other favourable factors, Taiwan becomes a rising market for private bankers in Hong Kong (Lo 1988).

** The stock market crash last October, discouraged many investors from entering the capital market, making them conservative on making new investment. At the same time, they become more aware of the consulting service offered by private bankers. There is increasing demand for private and professional services from HNWIs around Asia. Thus private banking will be benefited in long-term from the crash (Chan 1988, Ford 1987)

** The emigrations of Hong Kong investors to Canada and Australia also help the growth of private banking. The investors need to relocate their assets and make investment in countries that are new to them. They require expertise from an international bank to formulate the best arrangement for emigrations. American PBIs in Hong Kong thus launch products to cater for clients' needs³, while Australian and Canadian PBIs take this opportunity to expand their operations.

After listing some of the favourable factors for PBIs in Hong Kong, here are some of the threats faced by them.

** There are more and more competitions from both the existing competitors and new comers. The business of private banking is so profitable that banks rush to open their own PBIs to capture the growing market.

** The shortage of manpower is resulted from the emigrations of Hong Kong bankers and the increasing demand of personnels for expanded operations. Many banks face problems of recruiting good people on one hand and retaining them on the other hand. Though banks are willing to train up their own account managers, but find it hard to retain their trained staffs.

In short, private banking will see a continued growth for the coming years. A PBI should focus on evaluating its own strength and weakness and then formulating a competitive strategy to search for a sustainable favourable position in the industry.

The next chapter will exploit some conceptual frameworks of service marketing from the literatures reviewed by the author.

¹Most banks expect clients to have liquid assets exceeding US\$ 1 million to bank with them. Some banks do not insist on liquid assets if the clients' needs are assets management services.

²While for competitive reasons some of the details on growth rate and competitive advantages have been disguised, such changes have been kept to a minimum.

³CitiBank, Hong Kong launched Canadian Dollars Linked Certificates of Deposits and attracted over US\$ 50 millions from investors. Some of the investors are believed to be emigrants to Canada that use such CDs to hedge against their currency risk.

CHAPTER IV

MARKETING OF PRIVATE BANKING I --

UNDERSTANDING THE SERVICES AND CLIENTS' NEEDS

The purpose of this chapter is to offer the conceptual frameworks summarizing the unique characteristics of private banking as a service, the problems stemming from these characteristics and the strategies suggested as appropriate to overcome the problems. The ideas and concepts put forward in the books and periodicals will also be reviewed and summarized here.

4.1 Private Banking as a Service

Services have four characteristics that must be considered when designing marketing programs (Zeithaml et al 1985a).

Intangibility

Services are intangible. They cannot be seen, tasted, felt, heard, or smelled before they are brought. For example, HNWI's putting his money in a discretionary management fund cannot see the result before the end of the designated period. They should have faith in the PBIs and their account managers.

Inseparability

A service cannot exist separately from its providers,

whether they are persons or machines. A service cannot be put on a shelf and bought by the consumer whenever needed. The service requires the presence of the service provider. Financial advisory service requires the presence of both the client and his advisor to formulate the best financial plan for the client.

Heterogeneity

Services are highly variable - they depend on who provides them and when and where they are provided. The quality and essence of a service can vary from producer to producer, from customer to customer and from day to day. Thus PBIs having well trained account managers will have competitive advantages over other PBIs with less experience ones.

Perishability

Services cannot be stored. The perishability of services is not a problem when demand is steady, because it is easy to staff the services in advance. When demand fluctuates, service firms have difficult problems. For example, a PBI has to employ more account managers to cater for the sudden requirements of clients in different parts of Asia.

4.3 Marketing Tactics for PBIs

Here are some tactics suggested to solve problems stemming from the characteristics of private banking as a service.

Stress tangible cues.

PBIs offer some products with guaranteed returns, like fixed deposits, money funds and even gold or Canadian dollars linked Certificates of Deposits.

Simulate word-of-mouth communication.

PBIs target new clients mainly by referrals. They make great efforts to satisfy their existing clients and encourage them to tell their friends or relatives about PBIs' good services.

Create strong organization image.

PBIs from great names, like CitiBank, Chase Manhattan and Hongkong Bank, can easily establish confidence from their clients because of banks' good reputations. Swiss PBIs also have advantages because Swiss has long been famous for its private banking.

Use cost accounting to help set prices.

PBIs always find it difficult to set fee for their clients. Hongkong Bank's Private Banking department, for other reasons, does not charge its clients for the consulting services from the department. However, other PBIs need to set reasonable fees for their clients. Using cost accounting methods may be a feasible way to identify the bottom line of a PBI to offer a service.

Engage in post-purchase communications.

PBIs have to built a long-term relationship with their clients and rely on them to reach new clients. Thus,

they should engage in post-purchase communications, to strengthen their relationship with clients.

Emphasize selection and training of private bankers.

Since PBIs depends very much on their relationship with clients and account managers are the only channel to communicate with their clients, the selection and training of them is utmost important. To recognize such importance, some PBIs call their account managers as relationship managers. The so-called relationship managers should be suitably selected and well trained and have the right kind of personalities to help their clients.

Set up sub-offices in clients' home countries.

To better serve their clients, PBIs start to open offices in different parts of Asia. Though the account managers are Hongkong-based, offices in clients' place help to build confidence from clients. Recently many PBIs in Hong Kong set up new offices in Taiwan to cater for the increasing demands from Taiwan clients.

Industrialize or offer packaged products.

The reasons of offering packaged products are three-fold. The clients are more confident in buying the products because there are other users of the same products. The PBIs can have their fixed costs to share among a larger number of clients to attain low cost advantages. Some HNWIs prefer packaged products to tailor-made products for their small investments. Those HNWIs

are usually very rich and have much time to plan for their own investments.

Customize service.

Though packaged products are important in private banking, customize service or tailor-made products are equally important. HNWIs desire customized and personalized services and rely on PBIs to meet their specific financial needs. Without a personalized service, a client can never be a loyal and long-term customers for a PBI.

4.3 Understanding Clients' Needs

From the perspective of a PBI as a marketer, there are two generic marketing goals that serve as ends it would like to achieve. The two goals are the satisfaction of consumer needs, and the attainment of a competitive advantage over rivals (Bagozzi 1985). As the first step to attain these goals, a PBI needs both to understand clients' needs and to analyze competitors in private banking industry.

There are different ways to understand HNWIs' needs by looking from different perspectives.

Providing the right services.

Patrick Murphy explains how a buyer selects a product depending the type of that product perceived by him (Murphy and Eris 1986). The types of products discussed are convenience products, preference products, shopping products and specialty products (Diagram 4.1).

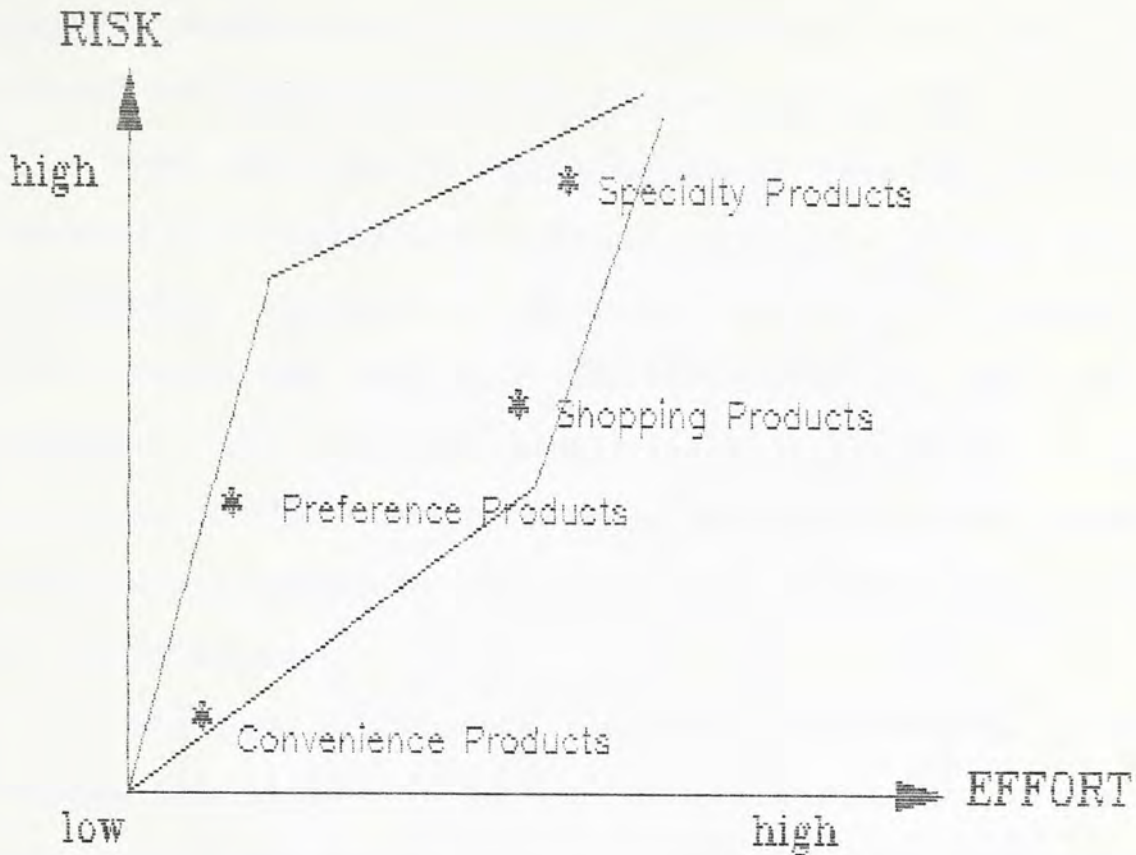


Diagram 4.1 Four types of Products

The classifications of products are in terms of effort and risk. For example, convenience products are defined as the lowest in terms of both effort and risk. The consumers will not spend much money on time in purchasing these products nor does he/she perceive significant levels of risk in making a selection.

HNWIs usually perceive a high risk on selecting a financial advisory service and try to spend much time and effort to select such a service. Thus, services from PBIs will never be considered as convenience or shopping products. They would be taken as preference products or specialty products. Taken private banking as preference products, HNWIs usually have preferences for specific banks but are willing to make substitution. Taken

private banking as specialty products, they no longer "shop" for alternatives but accept only one PBI.

Thus, for the benefits of PBIs, they should try to identify or cultivate clients with the perception of specialty products. Example of such clients are individuals who born poor and entrepreneured their way to wealth. They tend to remain heavily involved in their business and have little time or no time to spend studying which stock market or currency might yield the best return on their money.

PBIs' basic strategy should be high margin, limited volume and market niche. Products strategy is tailor-made, much resources support, guarantees and personalized service. Price strategy is negotiated price, while place strategy is exclusive and confidentiality. Promotion strategy is image building, personal selling and testimony.

Developing relationships with clients.

In Diagram 4.2, Robert Dwyer illustrates the importance of motivations in determining the relationship between buyers and sellers (Dwyer et al 1987).

A PBI should keep its clients' motivation high enough to sustain a relationship either as seller-maintained or, better, bilateral relationship maintenance. The motivation includes awareness of such a service, necessity of a personal advisor, a brand preference for a particular PBI and a perceived high quality of services.

Knowing the determinants of perceived service quality

can help a PBI to increase its clients' satisfaction on using its services, and thus to enhance their relationships (Zeithaml et al 1985b).

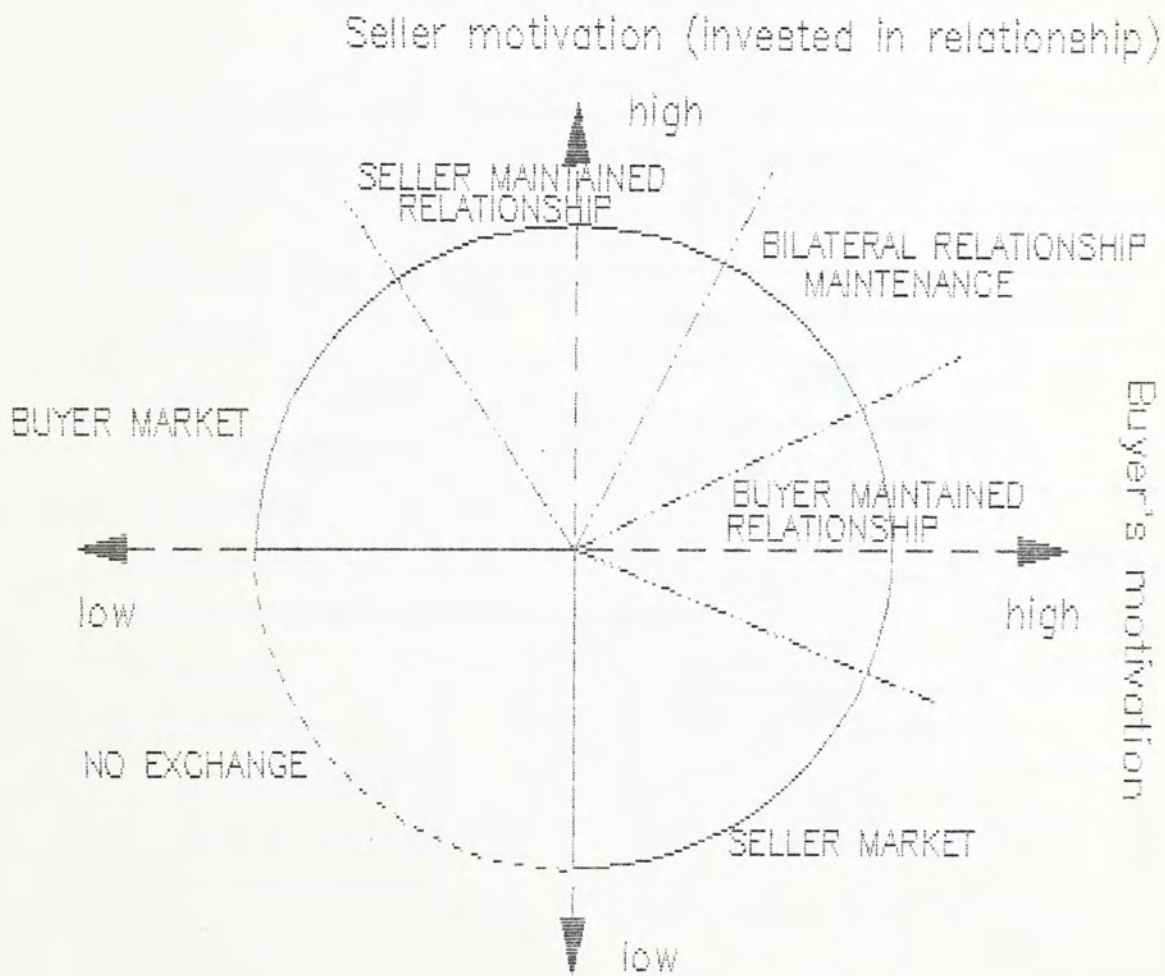


Diagram 4.2 The hypothesized realm of buyer-seller relationships

Perceived service quality is a function of perceived service and expected service. While there are many determinants of service quality, words of mouths, personal needs and past experience are very important to attain a high perceived service quality for a PBI (Diagram 4.3).

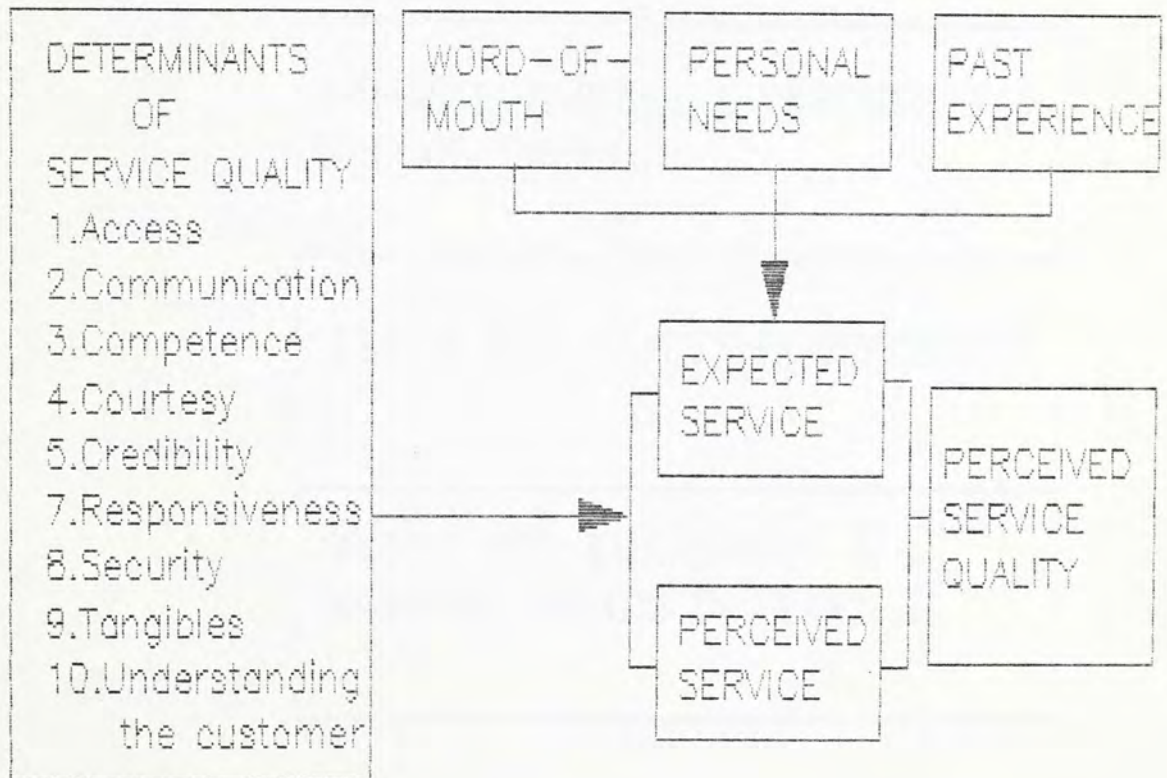


Diagram 4.3 Determinants of Perceived Service Quality

*Targeting the available Funds.*¹

When a rational man bets his fortune in horse races, he would not use the money for his food and housing. Thus a rational HNWI would classify his assets and funds into different levels of a pile of wealth (Diagram 4.4) and accept different risk factors (and liquidity levels) for different levels.

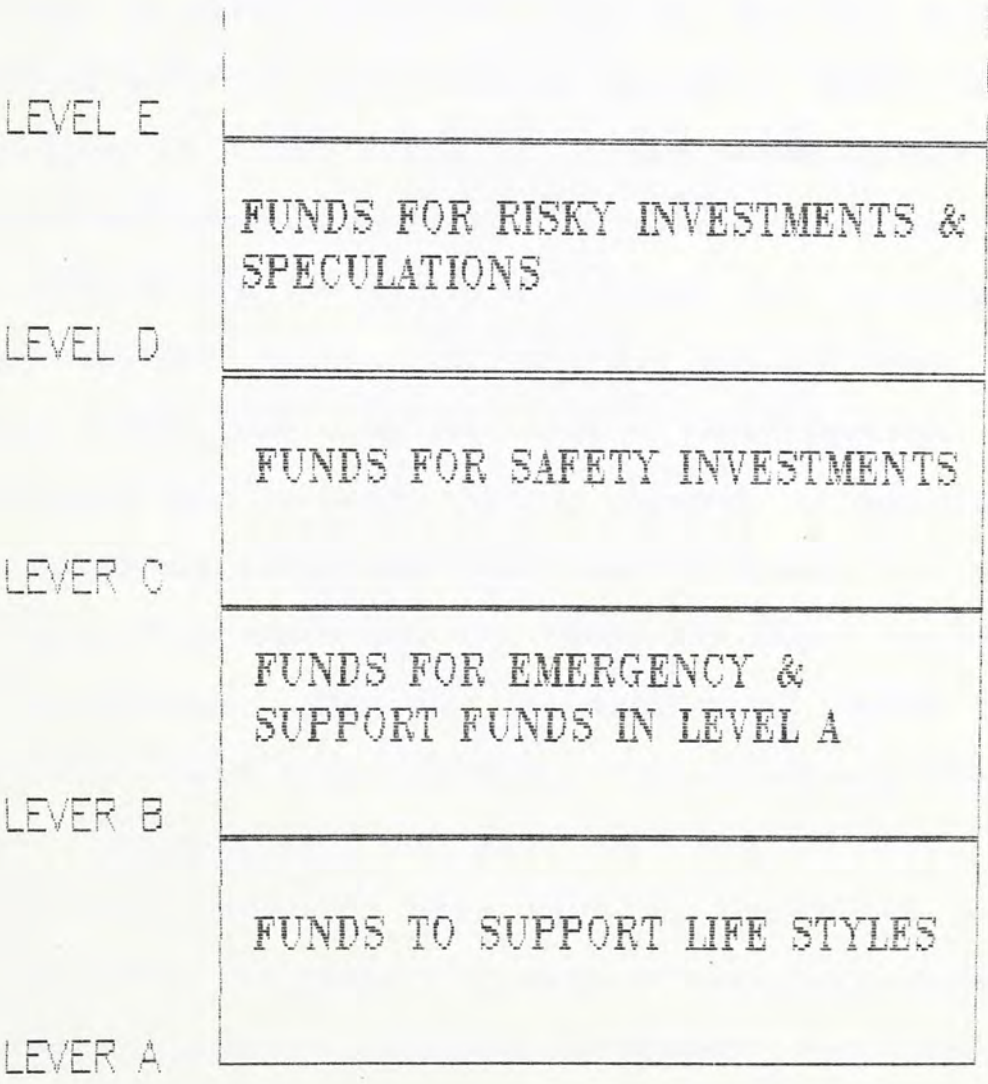


Diagram 4.4 A File of Wealth for a HNWI.

Level A is the most important one of a HNWI. They are funds to support their life styles and close relatives. They are the homes of HNWIs in the peaks and the funds for daily expenses. HNWIs would not accept any risk for this portion and demand high liquidity for these funds. Thus this portion is closed to private bankers for their investment products.

Level B is the next important one of a HNWI. They are funds to cover (back up) Level A. They are funds for emergency uses or from pension scheme. HNWIs usually place them in fixed deposits. They would accept small risk and try hard to preserve its value over times.

Level C are the funds available for investments. HNWIs would put it in a discretionary managed funds. They usually demand low risk and high diversification. Such funds would have no more than 40 percent in equities, so HNWIs would not panic when stock market crash.

Level D or above are the funds for risky investments and speculations. They are the easy money earned by the HNWIs from their main business. They would use the non-discretionary managed accounts provided by PBIs. They would accept relative high risk in expecting a high returns. They are usually clients of securities houses or investment companies offering investment services. They may open investment accounts with Wardley Investors Services or with Merrill Lynch.

There are many implications for PBIs in Hong Kong. When a PBI receive a fund from a client, it should

identify of which level the fund is belonging to. The level of that fund is also an indicator of its relationship with the client. Different PBIs should focus on absorbing funds from different sectors. While Merrill Lynch is aiming at funds from sector D or above, Bank of America aims at obtaining funds from lower levels from its more exclusive clients.

4.4 Knowing the Competitive Attributes

In the last chapter, the author has defined what is a PBI. Such definition serves not only as a qualification for a financial institution to be a PBI, but also as the scope for analyzing its competitors.

Knowing the scope of analysis is only the starting point to understand its competitors. The next step will be examining their attributes that help to attain their competitive advantages in private banking industry in Hong Kong.

There are five attributes that are most important for evaluating a PBI. They are its organization image, international networks, range of services, size of operations in Hong Kong, and country of origin.

Organization Image

Organization image means both the reputation and the perceived competence. Due to the very nature of private banking as a service, a good organization image is a prerequisite for building trust from a HNWI.

As forementioned, PBIs of great names have

competitive advantages over rivals. Examples are Private Banking Department of Hongkong Bank, Citi Private Bank, International Private Banking of Bank of America, and many others.

The perceived competence is the perception of HNWI's about the capacity of a PBI to provide a private and professional service. Thus a strong retail bank in Hong Kong without world-wide networks will find it hard to convince its clients about its competence as a private bank. On the other hand, a small but long-established Swiss bank in Hong Kong may attract clients with the perception of Swiss Banking as the origin of private banking.

International Networks

A PBI with international networks can deliver its private banking world-wide to its well-traveled clients. To provide a full range of private banking service, a PBI should have its private banking offices located in major investment centres, and its trust companies in "tax heaven" like the Cayman Islands and New Jersey.

A PBI can also be regional based. Canadian banks provide services to high net-worth immigrants to Canada while Australian banks attract would-be investors in Australia.

Range of services

A PBI can provide a full range of services or a narrowly defined service. It depends on the resources of the bank, the corporate and business objectives, the level

of commitment and its definition of business.

Merrill Lynch focus only on investment related services while Hongkong Bank can provide a full range services, from retail to fiduciary, from investment services to trust-setting, from estate planning to personal insurance.

Size of operation in Hong Kong

The size of operation of a PBI can be both an "asset" and a "liability" for it. A large size is an asset to provide a wide range of services, to provide packaged products, to win clients' confidence and to have a strong morale of its staffs. It is a liability because of its large overheads, high level of commitment and inflexibility to cater for changes in market needs.

Country of origin

Because of the culture difference, business philosophy of an American bank is quite different from that of a Swiss bank. American PBIs take pride in providing innovative products to their clients while Swiss PBIs stick to their expertise in the long established "Swiss Banking." A British clearing bank may have little motivation to expand its private banking services in Hong Kong, when an Canadian bank aggressively promote its private banking service.

To summarize the competitive attributes, a PBI can be described as either

** Well-known or Little-heard

- ** International or Regional
- ** Specialized in investment or Competence in all services
- ** Large or Small operation in Hong Kong
- ** American, Note-issuing, Swiss, European, or Others

After offering the conceptual frameworks summarizing the private banking as a service, needs of HNWIs and competitive attributes of PBIs, the next chapter will be devoted to the description of results of field studies.

¹Much of the ideas in this section are stimulated from an interview with Stanley Broderick of Bank of America.

CHAPTER V

THE MARKETING OF PRIVATE BANKING II -- KNOWING HOW THEY ARE DOING.

The purpose of this chapter is two-fold. Firstly, it will report the findings of field studies consisting mainly of in-depth discussions with the management of private banks in Hong Kong, concerning the problems they face and the marketing strategies they use to overcome them.

Secondly, it will compare the findings of field studies with the conceptual frameworks established in the last chapter.

5.1 Estimating the Market Size

The size of the market for PBIs in Hong Kong can be estimated by adopting a hypothesis that the wealth of people is distributed in a form of pyramid (Diagram 5.1). It illustrates that the more liquid assets a person has, the smaller portion of the population he belongs to.

The size of the market can be described by both the number of clients and potential business volume. After an estimation of potential market, the author will try to estimate the sizes of the available market, qualified available market, served market and penetrated market. (Kotler 1986, pp.246-247)

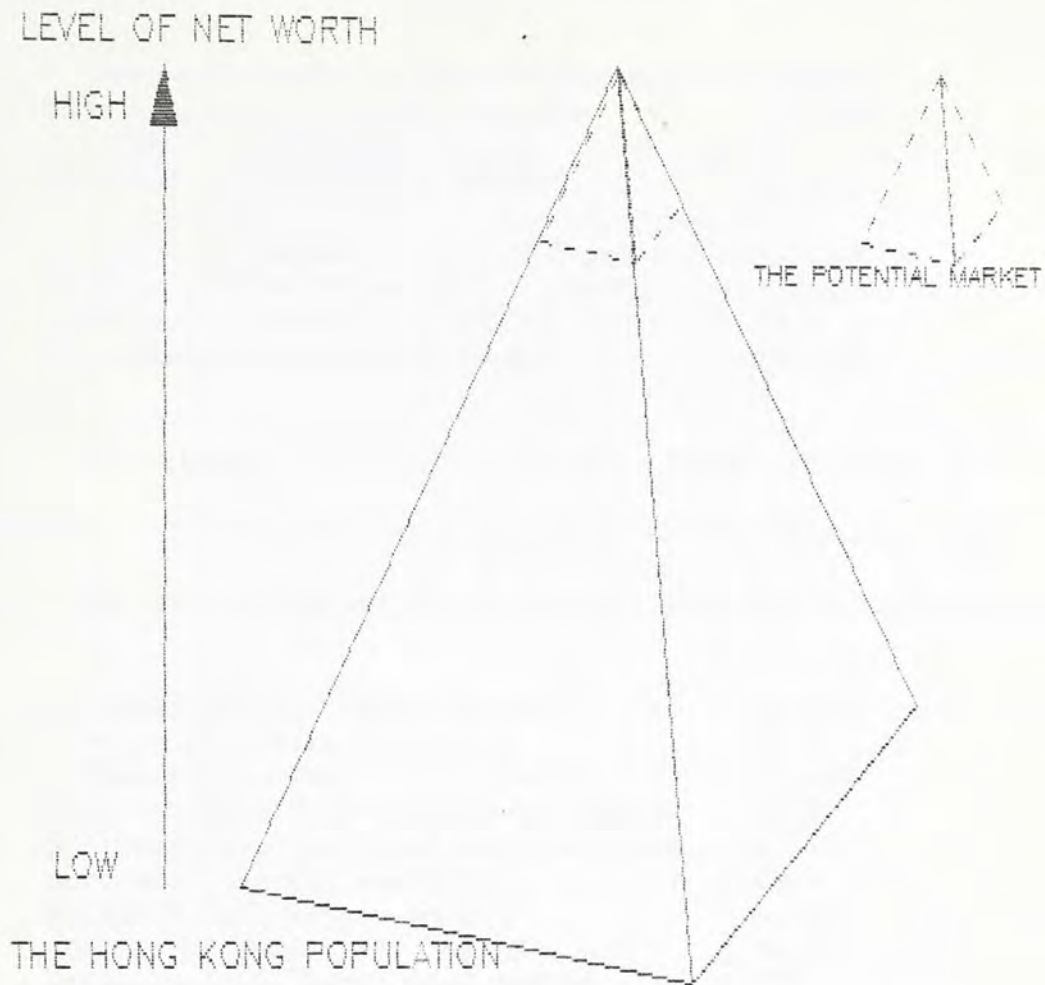


Diagram 5.1 A Model of the Distribution of Wealth

Firstly the author wants to estimate the potential market of HNWI's with liquid assets exceeding HK\$ 10 million. Here are some estimates of market in numbers of potential clients by different methods (data source : Hong Kong 1988).

1) Based on population (mid-1986).

| | |
|--------------------------------|------------------|
| Hong Kong Total Population | = 5,396,000 |
| portion of potential clients | = 0.5 % |
| Estimate (1), potential market | = 27,000 |
| | (No. of persons) |

2) Based on the labour forces (mid-1986).

| | |
|--------------------------------|-------------|
| Hong Kong Total Labour Forces | = 2,702,000 |
| portion of potential clients | = 1 % |
| Estimate (2), potential market | = 27,000 |

3) Based on the age group 35-64 (mid-1986).

| | |
|--|-------------|
| Hong Kong Total Population (age 35-64) | = 1,630,000 |
| portion of potential clients | = 1.5 % |
| Estimate (3), potential market | = 24,000 |

- 4) Based on number of private housing (mid-1987).
 Hong Kong Total Private Housing = 795,000
 portion of potential clients = 3 %
 Estimate (4), potential market = 24,000
- 5) Based on number of licensed private cars (1987).
 Hong Kong Total Licensed Private Cars = 146,000
 portion of potential clients = 15 %
 Estimate (5), potential market = 22,000

The above estimates range from 22,000 to 27,000 persons. To further our process of estimation, the author uses the mid-range as an estimate for potential market.

- | | |
|--|------------------------|
| Estimate (6), potential market | = 24,500 |
| portion of available market | = 50 % |
| Estimate (7), available market | = 12,300 |
| portion of qualified available market | = 50 % |
| Estimate (8), qualified available mkt. | = 6,100 |
| portion of served market | = 50 % |
| Estimate (9), served market | = 3,100 |
| portion of penetrated market | = 30 % |
| Estimate (10), penetrated market | = 900 |
| average business volume | = HK\$ 100 mil. |
| Estimate (11), penetrated market vol. | = HK\$ 90,000 mil. |
| <i>compared with :</i> | |
| Deposits with all deposit-taking companies (1986) | = HK\$ 59,298 million |
| Deposits with all deposit-taking institutions (1986) | = HK\$ 550,651 million |

Summary of estimates :

Potential market of HNWI's with liquid assets exceeding HK\$ 10 millions is 24,500 persons.

50 % of which have interest in using service from PBIs, or the available market is 12,300 persons.

If the PBIs expect further qualifications from the HNWI, like good sources of money, non-US citizens or local Chinese, the qualified available market will be around half of available market, i.e. 6,100 persons.

If a PBI concentrates on certain segments, for instance, HNWI's with assets exceeding HK\$ 50 millions, the served market will be 3,100 persons.

Assuming the PBI and its competitors have already reached 30 % of the served market, the penetrated market is 900 persons.

If the average business volume of such HNWIs is HK\$ 100 millions, the penetrated market in dollars terms is HK\$ 90,000 millions, which is the funds deposited in or managed by the PBIs in Hong Kong for HNWIs of liquid assets exceeding HK\$ 50 millions.

The above is an attempt by the author to estimate the market size for a PBI with target market of HNWIs of liquid assets exceeding HK\$ 50 millions. The estimates are quite realistic when compared with a PBI's estimate of the *Hong Kong total* market size of 3,000 persons and another PBI's estimate of *its own* business volume in 1988 of US\$ 600 million.

A PBI with its own proprietary information will have a much better estimation of the market size. Compared with its own number of clients and business volumes, it can also estimate the market share of the firm.

5.2 Targeting New Clients

An old wisdom in private banking states that account managers from good families can be a good lead for new clients. Their good ties with rich people will help a PBI to reach new clients and enlarge its business volume.

However, it may not be applicable now. Some HNWIs from large families usually do not want to bank with their relatives or relatives of their close friends just to prevent others knowing their wealth. There are also a lot of HNWIs who were born poor and entrepreneured their ways to rich. They would prefer to bank with experienced and hard working private bankers than to young guys from rich families.

PBIs in Hong Kong depend much on referrals for new clients. Around half of their new clients are from referrals. It seems to agree with conceptual framework built in the last chapter that service marketing rely on

referrals, word-of-mouth communications and testimony.

PBIs usually keep a list of their target clients. They identify them by scanning memberships of some exclusive clubs and by market intelligences. However, they never make plain cold call to these clients. They would instead identify potential clients' business partners that the PBIs know well. They then get in touch with these clients by introduction from those businessmen.

Other targeting methods are upgrading of clients from investors-related services or personal banking, advertising for packaged products, and joining the social circles of HNWIs. Those new clients are usually the "newly-rich" entrepreneurs who experienced a sharp rise in their wealth resulted from the recent success in their business.

5.3 Selecting and Training the Account Managers

Many PBIs in Hong Kong contributes their success in recent years to their good staffs. They are particularly happy with the performances of their accounts managers. However, they are equally unhappy with the leave of their good people and the difficulty of recruiting a good account manager.

PBIs are very demanding on the quality of their accounts managers. They expect them to have very good interpersonal skills, solid knowledge of capital market and other investment products.

While some PBIs require mature account managers with ages over thirty, others stress more on knowledge and

hard-working. The different requirements appear to depend on the different clients bases of the banks. While the former have conservative clients with ages over fifty, the latter have less conservative investors with ages around forty.

Because of the shortage of experience bankers, many PBIs start to train up their own staffs for the posts of account managers. However, they are sometimes frustrated by the leave of their newly trained-up account managers. It is always unavoidable in such a fast growing industry like private banking.

5.4 Offering the Best Products

Private Banking services include three categories of products. The first type is standard products. These products are actually an extension from retail banking. They include standard banking services, investment services, Swiss banking, insurance, fiduciary services and trusts. They are the basic products usually needed by general clients. However, a PBI can hardly differentiate itself from its competitors by offering only standard products.

Thus as the relationship between the PBI and its client becomes closer, the PBI will tailor-make their products for the client to meet his specific financial needs. The client will then stop "shopping" for alternatives but accept only one PBI. The PBI has actually strategically moved its products type from preference products to specialty products (see "Providing the right

services" in the last chapter)

On the other hand, many PBIs would like to offer packaged products. Packaged products of Citi Private Bank includes Citifunds and Citiplus accounts, Index, gold or Canadian dollars linked Certificates of Deposits.

Citibank is famous for its innovative packaged products. There are a lot of reasons resulting this behaviors. Citibank is aiming at a larger customer base than Bank of America. It uses packaged products to target their new customers and share its high cost of maintaining a strong team of financial specialists. Its corporate culture encourages innovations among its staffs. Advertisement for subscription of innovative packaged products in newspapers will also help its image building.

Emigration advisory service is a ticket for a new PBI to enter the growing market of private banking. They are using market-niching strategy by satisfying particular needs of the market. Their competitive attribute (see chapter VI) over existing PBIs is their expertise in their home countries to where their clients emigrant. Examples are Canadian banks and Australian banks.

In short, a PBI can offer its best products to its clients in different ways depending on its size of target market, its strength and weakness, and also the opportunities of the market.

5.5 Employing the Right Promotion Effort

Many PBIs in Hong Kong hesitate to place advertisement in newspapers as they doubt the

effectiveness of the advertisements. Another reason for not placing advertisements is the low profile of the PBIs and their stress on exclusiveness of services.

However, others PBIs rely on advertisements to fulfill several objectives, namely, to build their image, to reach new clients, to make them be known for their private banking services, and to sell their packaged products.

Advertisements for packaged products and for general private banking products are usually placed in Chinese financial newspapers and magazines. They are targeting the local chinese with little awareness of the private banking service provided by PBIs.

Advertisements for banks image are usually placed in international English business magazines, like Far East Economics Review and Economists. In those advertisements, PBIs only present their business philosophies or concepts rather than their products.

In addition to image building, other promotion efforts are personal selling and testimony. It confirms the promotion strategy proposed for speciality products described in the last chapter.

5.6 Developing Growth Strategies

Many PBIs in Hong Kong have great confidence on the future of private banking. They foresee a continued high growth of the industry. However, there are also threats from substitutes and new comers. Thus all the PBIs in Hong Kong are employing some sort of growth strategies.

They also set a very high objectives for their growth of business.

To meet their growth objectives, different PBIs use different strategies (Ansoff 1957). Most of them use market penetration strategy. They seeks increased sales for its current services in current markets through more aggressive marketing effort. The effort includes heavy advertising, cold call by introduction and develop existing clients for larger business volume.

Other PBIs also engage in market development. For example, many PBIs open offices in Taiwan to exploit the untapped market (Lo 1988). Some PBIs use packaged products to develop new markets. Examples are emigration advisory services and Canadian dollars linked CDs.

The third growth strategy used by PBIs in Hong Kong is product development. Citibank develop gold linked CDs when their existing clients demanding such a product to take advantages of the rise of the price of gold without holding gold. In doing so, Citibank not only satisfy its clients' needs but also attract new clients from its target market.

In the next chapter, the author will summarize the strategies suggested in chapters IV and V. The author will also offer recommendations, by exploiting alternatives of generic marketing strategies and feasible marketing approaches.

CHAPTER VI

RECOMMENDATIONS FOR PRIVATE BANKING IN HONG KONG

The purposes of this chapter are (1) to summarize the marketing tactics and strategies suggested in the last two chapters, (2) to offer recommendations, by exploiting alternatives of generic marketing strategies and feasible marketing approaches. It is hoped that the recommendations can contribute the further development of the private banking industry in Hong Kong.

6.1 Marketing Tactics for Private Banking as a service

Private banking as services have four characteristics that must be considered when designing marketing programs. They are intangibility, inseparability, heterogeneity and perishability.

There are also five competitive attributes of a PBI to attain competitive advantages over its rivals. They are organization image, international networks, range of services, size of operation in Hong Kong, and country of origin.

The marketing tactics suggested for PBIs are

Products tactics

- 1) Stress tangible cues.
- 2) Offer packaged products
- 3) Customize services.

- 4) Classify the services as speciality products

Pricing tactics

- 5) Use cost accounting to help set prices.
- 6) Adopt negotiated prices.

Place tactics

- 7) Stimulate word-of-mouth communication.
- 8) Engage in post-purchase communications.
- 9) Emphasize selection and training of private bankers.
- 10) Set up sub-offices in clients' home countries.

Others tactics

- 11) Create strong organization image.
- 12) Increase clients' motivation in consuming PBIs' services.
- 14) Analyze the pile of wealth of the HNWIs.
- 15) Encourage more referrals from existing customers.

There are also three growth strategies available for PBIs. They are market penetration, market development and product development.

While all PBIs can adopt most of the tactics suggested above, different PBIs with different competitive attributes should employ only those growth strategies that match their objectives and resources.

For example, a well-known, international investment bank with large operation in Hong Kong can use all three growth strategies. At the same time, a little-known, regional commercial bank with small operation in Hong Kong usually adopts market penetration as growth strategy.

6.2 Choosing the Right Marketing Strategies

When choosing marketing strategies for a PBI, it need to evaluate its company's objectives and resources.

Every bank pursues a set of objectives based on its missions and business scopes. A PBI within a bank should recognize those missions and business scopes. For example, some banks may demand its strategic business unit not to grow too fast or it will be out of control. Thus its PBI should adopt a growth strategy that attain a growth rate that are desired by the bank.

To succeed in private banking, a PBI needs a lot of resources to capture the market and earn a profit. It may force some PBIs to adopt market niching strategy to lessen their resource requirements.

On the contrary, CitiBank, for instance, has a lot of resources to support its private banking offices. Its private banking offices can thus afford to serve a wide range of clients and offer them either tailor-made and packaged products depending on clients' needs.

In short, a PBI should evaluate its company's objectives and resources before adopting any marketing strategy.

6.3 Three Generic Marketing Strategies

Michael Porter suggested three generic marketing strategies for marketers to achieve the goals of customer satisfaction and competitive advantage (Porter 1980). They are product differentiation, overall cost leadership and market focus.

Product Differentiation

The strategy of product differentiation aims to market a product or service that is perceived by customers to be unique in some way. A Swiss bank may convince its client about their expertise in Swiss Banking while an American Bank may differentiate itself as an investment expert with international infra-structures.

Overall cost leadership

Although all PBIs try to keep costs to a minimum, not everyone makes it a top priority. Other strategies sometimes take precedence. For example, certain PBIs that choose a differentiation strategy find that they must house a strong team of financial specialists to improve their service quality as well as spend extra money on advertising or promotion. These PBIs obviously have spending limits but differentiation objectives are met first. In contrast, when a PBI makes cost cutting as its primary goals, we may call this overall cost leadership.

Market Focus

This strategy aims to concentrate on a particular subdivision (or segment) of the market, such as a specific type of services or group of clients. For example, Bank of America may find it necessary or advantageous to pursue selected segments of HNWI's with liquid assets exceeding US\$ 5 million rather than a larger market as defined by the other PBIs. At the same time, Canadian Banks focus on their emigration advisory services to enter the market and

try to dominate in this particular small segment of private banking. Overall, the goal of market focus is to discover a segment (or small numbers of segments) and dominate and defend it against competitive threats.

6.4 Four Marketing Approaches

Before making the final recommendations to PBIs in Hong Kong, the author would like to exploit four feasible marketing approaches available to them. They are service niching approach, pro-active approach, second-in approach and inactive approach.

Service niching approach.

The PBI with this approach attempts to locate and maintain a service niche in a relative stable products or services area. The PBI tries to offer a more limited range of products or services than its competitors and it tries to protect its domain by offering higher quality, superior service, lower prices. However, the PBI is not at the forefront of developments in the private banking industry. It tries to ignore industry changes that have no direct influence on current areas of operation and concentrates instead on doing the best job possible in a limited area.

This is the usual approach adopted by small PBIs or new comer to the market. The risk factors are low and the returns are reasonable. However, in a fast-growing market of private banking, being stable may mean losing market share quickly and hence endanger its long term profitability.

Pro-active approach.

The PBI with this approach typically operates within a broad product-market domain that undergoes periodic redefinition. The PBI values being first in new product and market areas even if not all of these efforts prove to be highly profitable. The organization response rapidly to early signal concerning area of opportunity and these responses often lead to a new round of competitive actions. However, this PBI may not maintain market strength in all area it enters.

As the risk factors are high in this approach, the expected returns may be the highest of the four approaches. On the other hand, there are many intangible benefits, like good image of the PBI, high morale of its staff. However, not all PBIs can adopt this approach because of their limited resources available.

"Second-in" approach.

The PBI attempts to maintain a stable limited line of products or services while at the same time moving out quickly to follow a carefully selected set of the more promising new developments in the industry. The PBI is seldom "first-in" with new products or services. However, by carefully monitoring the actions of major competitors in areas compatible with its stable product-market base, the PBI can frequently be "second-in" with a more cost efficient product or service.

The advantages of this approach is low risk and sure return for its resources employed in the development of

products. Its disadvantage is its lower class and copy-cat image which may not be compatible with its corporate image in other sectors of the banks.

Inactive approach.

The PBI does not insist on any product-market orientation. The PBI is not aggressive in maintaining established products and markets. It would not take any undue risks to develop new products. The PBI responds only in those areas where there is enough environmental pressure.

The advantage of such a approach is the risk factors is the lowest but the expected returns would also be the lowest.

6.5 Recommendations to PBIs in Hong Kong

Due to the intrinsic difference among PBIs, there is no one and only one strategy that is applicable for all PBIs in Hong Kong.

However, out of the three generic strategies, overall cost leadership seems to be the least appropriate. PBIs in Hong Kong should use a combination of product differentiation and market focus. The private banking is a fast growing industry and demanding high quality services. Thus a PBI with plenty of resources should employ product differentiation while one with limited resources or a new comer should employ market focus.

Similarly, PBIs with large resources and high corporate image should adopt pro-active approach or

service niching approach. While small banks with limited resources 'should adopt "second-in" approach or even inactive approach.

In short, a PBI should review its proprietary information, its company's objectives and resources before coming up with the best approach or strategy.

In other words, by revising the competitive attributes of a PBI, it can select a generic marketing strategy. Then the PBI can fine tune its existing marketing approach to be more effective in attaining its objectives.

6.6 Concluding Remarks

This study adopts a marketing management approach to analyze the private banking industry. The issues selected to include in the study are related to the author's belief that the key to achieving organizational goals consists of determining the needs and wants of target markets so delivering the desired satisfactions more effectively and efficiently than competitors.

It is hoped that through a better understanding of the needs and wants of private banking market and the characteristics of the market, a PBI can create exchange that satisfy both HNWI's and PBI's objectives.

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